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Executive Secretary
9/20/83
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THE SECRETARY OF THE TREASURY

WASHINGTON, D.C. 20220

September 20, 1983

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(With ~~Confidential~~ Attachment)

MEMORANDUM FOR THE VICE PRESIDENT
THE SECRETARY OF STATE
THE SECRETARY OF DEFENSE
THE SECRETARY OF AGRICULTURE
THE SECRETARY OF COMMERCE
DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET
✓ DIRECTOR OF CENTRAL INTELLIGENCE
UNITED STATES TRADE REPRESENTATIVE
ASSISTANT TO THE PRESIDENT FOR
NATIONAL SECURITY AFFAIRS
ASSISTANT TO THE PRESIDENT FOR CABINET AFFAIRS
CHAIRMAN, COUNCIL OF ECONOMIC ADVISORS
ASSISTANT TO THE PRESIDENT FOR POLICY DEVELOPMENT

SUBJECT Senior Interdepartmental Group on
International Economic Policy (SIG-IEP)

A meeting of the SIG-IEP is scheduled for Friday, September 23, at 3:00 p.m., in the Indian Treaty Room (Room 474, Old Executive Office Building). The agenda is as follows:

1. Role of U.S. Government Export Credits and Guarantees in Response to International Debt Problems,
2. East-West Economic Relations, and
3. Export Administration Act.

An IG paper on agenda topic 1 was circulated on August 10; a paper on topic 2 is attached. Background for discussion of topic 3 will be an oral report.

Attendance will be principal, plus one.

Donald T. Regan

Attachment

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Ongoing East-West Economic
Study and Work Program

Overview

Introduction

This package is designed to report on the East-West economic study and work program presently being pursued under the mandate of NSDD 66. The overall goal of the program is to keep up the considerable momentum achieved during the first six months after issuance of the NSDD in highlighting the security implications of East-West economic relations and in encouraging U.S. allies and partners to take a stronger line in their economic relations with the East.

This overview surveys the entire program and calls particular attention to the interrelationships between various segments of the program, while the papers that follow present more detail on each major element.

Overall Program Objectives

1. To promote development of Western energy resources, and especially North Sea natural gas, as economically viable alternatives to excessive Western European dependence on Soviet gas.
2. Within the context of work on general security of energy supply, strengthen Western energy security against possible disruptions in Soviet supplies in particular.
3. To assure that such foreign trade as is conducted with the Soviet Union and Eastern Europe is advantageous to the West and does not undermine Western security by helping the Soviets develop their military capabilities.
4. To assure that no preferences are accorded in trade with the Soviets while working with other countries eventually to eliminate subsidization of credit in trade among all developed countries.
5. To continue to monitor closely, and study a variety of aspects of, East-West economic relations in order to develop the bases for common allied, or more broadly Western, approaches to these relations in the future.

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Ongoing East-West Economic
Study and Work Program

NATO

Objectives

Our primary objective is to focus the NATO Economic Committee's analytical work on those aspects of East-West economic relations identified in the Committee's recent study as having the most important security implications for the Alliance (high technology transfer, energy dependency, financial relationships). This represents a continuation of our efforts to shift the emphasis in the Committee's work away from its traditional preoccupations with questions of CMEA development and the outlook for economic reforms in the USSR and Eastern Europe. We will also want to ensure that, when appropriate, significant East-West economic issues are included on NATO Ministerial agendas, with Economic Committee reports available for the ministers on these issues. However, since the INF issue can be expected to dominate discussions at the December ministerial, it would be prudent to postpone ministerial consideration of contentious economic issues until the Spring 1984 ministerial.) 7

Work Program

The NATO Economic Committee's work plan for the coming year includes Committee meetings, reinforced by national experts, on those particularly significant aspects of East-West economic relations identified in the Committee's recent study. The more important meetings, which will include an examination of the security implications of each issue, are:

- October: Convertible Currency Balance of Payments of the USSR and Eastern Europe

At this meeting, national experts will review recent trends and short-term prospects of convertible currency balance of payments and indebtedness of the USSR and EE countries and will weigh the relevant security implications for the Alliance. Our objective for this meeting is to produce a solid analytical paper which bolsters the stated position that it is not in the Alliance's interest to provide preferential financial terms to the Soviet Union. A follow-up meeting is

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tentatively scheduled for May 1984. If, after the October meeting, we consider it appropriate to include this issue on the agenda for the Spring ministerial, we may want to propose a policy-level discussion of the issue at the May committee meeting.

-- January: Soviet Industry

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The terms of reference for this study are still under discussion, and one of our main goals will be to ensure that they turn out as we wish. We have proposed a series of studies on the development of key Soviet industries, including high technology sectors, which contribute significantly to Soviet military capabilities. Our objective for this study is to evaluate the contributions made by Western technology to the development of these key industrial sectors and to highlight the importance of keeping trade relations with the Soviet Union consistent with allied security concerns. This would support and complement our effort in COCOM. We envision a long-term study program that would involve several meetings and committee papers over the next two years, with emphasis on important high technology sectors such as microelectronics and telecommunications. We intend to provide the committee with a paper on the microelectronics industry in the Spring. We face difficulties, however, since France is willing only to accept a general study of Soviet industry, adamantly arguing that high technology issues should be addressed only in COCOM. We will continue to press for acceptance of our proposal, but French intransigence may inhibit, at least temporarily, meaningful work on this topic.

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-- February: Soviet and East European Energy Production and Requirements

The purpose of this meeting would be to develop a common Alliance assessment of Soviet energy prospects and policies, including an examination of Alliance dependence on Soviet exports. CIA is preparing a National Intelligence Estimate (NIE) on Soviet energy policies and prospects through the 1990s. The NIE will assess the possibilities for Soviet production, consumption, and foreign trade for each major form of energy. It will examine possible alternative Soviet energy policy strategies and consider how different strategies might affect Western interests and how Western actions

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might affect the choice among energy strategies by the Soviet Union. A US paper, based on the NIE, will be provided to NATO as a US contribution to its study.

- April: NATO Economic colloquium. The annual colloquium provides an excellent opportunity for us to submit papers on, and stimulate discussion of, several key issues in support of the inter-governmental efforts we are undertaking in both NATO and elsewhere. We are pursuing efforts to stimulate the preparations of papers on the following topics: Economic Reforms under Andropov; 1983 Soviet Economic Performance; Problems and Prospects in Soviet Industry; Soviet Energy Prospects and Problems; Resource Allocations: Military vs Civilian; Technology: Development, Diffusions, and Dependence.

Policy-level discussion of the Economic Committee studies can be scheduled, when appropriate, in either the Economic Committee or the North Atlantic Council (NAC). East-West economic issues that merit ministerial consideration can be included on the December 1983 or Spring 1984 ministerial agenda, as appropriate.

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Ongoing East-West Economic
Study And Work Program

COCOM

Objectives

U.S. objectives over the next year for COCOM Fall into the following four areas:

1. List Review -- We will push hard for acceptance of seven of our high priority items as well as for the remainder of our List Review proposals. Difficulty is expected in the area of robotics and in computers.
2. Harmonization of Licensing and Enforcement -- We plan to highlight the general need for a consensus on enhanced vigilance toward violations of export controls; we will also seek to formulate recommendations toward improved monitoring of strategic goods to third countries, more extensive use of "binding" end-use certificates, and approaches to non-COCOM countries to encourage a tightening of their export control practices on commodities originating in COCOM countries.
3. Technology Controls -- We will seek to persuade the French to accept the German proposal for a separate technology control list; we will push for implementation of the proposal to monitor emerging technologies, already agreed in principle; and we will continue to press for our oil and gas proposals, which so far have met considerable resistance. 7
4. Strengthening of COCOM -- We will push forward with our ongoing efforts, which include a provision of additional funding for translators and equipment (including word processors); implementation of a weekly courier service between Paris and the Office of East West Trade; FY 84 commitment of \$2 million from the DOD budget for COCOM space and personnel improvements.

Work Program

Our initiatives in the List Review will be carried forward when the Review resumes in September; contentious issues not resolved this Fall will have to be carried over for additional talks next spring.

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On Harmonization of Licensing and Enforcement, the Subcommittee on Export controls will meet on September 26 to review actions taken by national authorities. We plan to use this meeting to press our views in this area and as a starting point for an ongoing process in these areas.

In the area of technology controls, we will begin work immediately to persuade the French to accept the German proposal for a separate technology control list. On the effort to monitor emerging technologies, we will be preparing positions for a January, 1984, meeting to discuss modalities for implementing this proposal. On our oil and gas proposals, four items have been folded into the list review process that resumes this month, while the remainder will be discussed at a January 10-12 meeting of the ad hoc group.

On strengthening COCOM, we plan this Fall to install a Wang word-processing system, implement a weekly courier service, and commit the funding of \$2 million from Defense.

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Ongoing East-West Economic
Study and Work Program

OECD

Objectives

At their May 1983 meeting, the OECD Ministers agreed that the organization had carried out a thorough economic analysis of the evolution of the West's trade and financial relations with the USSR and Eastern Europe and should continue its review of developments in this area. Our main task in OECD will be to sustain the momentum achieved last year. We have considerably raised the visibility of East-West issues in the organization as a whole, and in the coming months, we will want to build upon this work by seeking to sustain the momentum provided by the Ministerial.

The importance we attached to the OECD's work on East-West issues is based on the fact that it should provide a means for developing a consensus on, or at least advancing the member governments' understanding of, the economic aspects of East-West relations -- which complements work on security/political issues in NATO, energy concerns in the IEA, and technology transfer objectives in COCOM. Within the various organs of the OECD, we are pursuing the following objectives:

In the XCSS, we will try to ensure that East-West issues receive the same high level attention and political directions that they have in the recent past.

In the Committee on Financial Markets, we will explore with the Secretariat ways that this Committee or its subgroups can integrate Trade and finance work in the East-West area. One is to make permanent an existing ad hoc group of East-West financial experts and provide for it to meet jointly with its counterpart from the Trade Committee.

In the Trade Committee, we will try to achieve a better integration of trade and finance considerations, supplemented by in-depth studies of economic, trade, and financial considerations in individual Eastern countries. Also in the Trade Committee, we will push for the Committee to carry out its Ministerial mandate to investigate the balance of advantages in East-West Trade, focusing on countertrade and the monopsonistic advantages of Eastern state trading companies.

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These objectives will be implemented during the coming year through work programs in NATO, IEA, OECD and COCOM. The attached papers survey the broad outlines of these work programs. The working groups established in NSDD 66 will be responsible for developing detailed strategies and tactics for the conduct of the studies and negotiations described in these papers.

In broad terms, particular objectives defined above will usually be pursued simultaneously in more than one forum.

Objective 1 will be implemented through action in the IEA, NATO (the study on Soviet energy prospects) and bilaterally with various countries.

Objective 2 will be implemented primarily through the IEA country review process, supplemented bilaterally where appropriate.

Objective 3 will be implemented through our work programs in COCOM, NATO and OECD, and is intended to increase allied and Western sensitivity to the need to improve and expand controls on exports to the Soviets and Eastern Europe and increase Western resistance to foreign trade practices which have undesirable trade policy consequences for the West.

Objective 4 will be implemented primarily through on-going negotiations for renewal of the OECD Arrangement on Export Credits, supported by bilateral efforts with particular countries as needed and by continuing work on East-West economic relations in OECD.

Objective 5 will be implemented in OECD and NATO as regards both improvement of data collection and analysis and the various study programs in the two institutions.

Successful achievement of our objectives will require close coordination among the individual programs to assure that efforts in each are orchestrated to be mutually reinforcing. NSDD 66 designates the SIG-IEP as the primary coordinating mechanism at the policy level, and the Under Secretary of State for Economic Affairs is the SIG-IEP coordinator for East-West economic relations. The Under Secretary or his Deputy is responsible for day-to-day coordination among the various NSDD 66 Working Groups, working closely with NSC staff.

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In the OECD-BIS collaborative effort, our goal is to upgrade the data that the two organizations collect by consolidating the information and avoiding double counting. We will monitor and encourage this effort, which is now on track.

In the Export Credit Arrangement, we will be working to stiffen the terms applicable to category I countries, and eventually to eliminate subsidization of credits or guarantees.

Work Program

1. OECD Executive Committee in Special Session (XCSS) -- We have made East-West de facto a virtually permanent issue of discussion at XCSS meetings. We should try to ensure that it continues to receive XCSS attention sufficient to give the necessary political direction to efforts of the Secretariat and committees on a continuing basis.
2. Trade Committee -- The Trade Committee oversees the preparation of a semi-annual report on current developments in East-West trade and finance. Our main goal here is to achieve a better integration of trade and finance considerations. Such an integrated analysis is essential to understanding the dynamics of East-West developments (see also No. 3). These reports should also continue to be supplemented with in-depth studies of economic, trade, and financial conditions in individual Eastern countries.
3. Committee on Financial Markets (CFM). -- The CFM is planning to upgrade its input into the Trade Committee's East-West report. An ad hoc sub-group of East-West financial experts will meet in October to get a Secretariat report on East-West financial developments which will feed into the Trade Committee's effort. This scheme is a possible step toward a solution to the problem we have had with integrating trade and finance work in the area. Consequently, our goal here is to explore with the Secretariat the potential for giving this sub-group a more permanent status and expanding its role, for example, by having it meet jointly with the trade Committee's Working Party on East-West trade.
4. Balance-of-Advantages -- We also want the Trade Committee to carry through on the mandate given to it by the Ministers to investigate the balance-of-advantages in East-West trade, with a view especially to delineating the monopsonistic advantages of Eastern state trading companies in dealing with

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Western firms and the use of countertrade practices by the Eastern countries. We should also continue to push the idea of an exchange of information/early warning system on major projects to the East. We will aim at least for an agreed outline by spring and a first draft of a report by a year from now.

5. OECD-BIS Collaboration -- The goal of this exercise is to consolidate the data collected by the two organizations, in the process eliminating double-counting of official and private credit flows, so that comprehensive, integrated debt and financial flow statistics can be obtained. It appears that this project is well on track, but we will continue to monitor progress on it.

6. Export Credit Arrangement -- Our effort in the Arrangement should be evaluated separately from those (Nos. 1-5) concerned with monitoring economic and financial developments. In the Arrangement we have taken care not to argue that the USSR or other Eastern countries should be singled out for more stringent treatment. Rather we have pushed for tighter terms to all Category I countries, which coincides with our broader Arrangement goal of reducing credit subsidies. Since the EC did not accept the Export Credit Group Chairman's compromise ("Wallen II"), the current Arrangement provisions have been extended until October 31, 1983. With or without Wallen II, the considerable improvements we achieved last year in treatment of Category I countries will still be retained. We will continue to work to stiffen further Category I terms.

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Ongoing East-West Economic
Study and Work Program

Energy Requirements

Objectives

The follow-up to the Energy Requirements Study places particular emphasis on the security of gas supplies to Europe, and the need to find economical alternatives to Western European dependence on Soviet gas.

Specific objectives include supporting the development of Norway's Troll gas field, encouraging France and Germany to continue their efforts to minimize their reliance on Soviet sources of energy, and encouraging Sweden to look to Norway rather than the USSR for its future gas needs.

Work Program

IEA

Formal follow-up to the Energy Requirements Study began with a meeting of the IEA's Standing Group on Long Term Cooperation (SLT) on July 20. The SLT meeting went very well, indicating that European countries will agree to a serious and sustained IEA involvement in natural gas security issues. The principal item on the agenda was to agree to a program of work for the IEA Secretariat to follow up on the May Ministerial. The SLT approved the Secretariat's proposed program of work without significant changes. The work program includes existing Secretariat projects in the areas of oil, coal, price and investment policies as well as the following new work in the gas area:

- Use of country reviews to examine indigenous gas development opportunities, supply scenarios, and gas production and disruption contingency plans.
- Preparation by the Secretariat of background papers on gas security issues in each IEA member country.
- The Secretariat will give special attention to selected gas alternatives, including Troll, North America, North and West Africa, the Middle East and Iran.
- The Secretariat will take "particular note" of developments which either increase or decrease vulnerability.

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- The Secretariat will look specifically at barriers to trade in natural gas in the context of a general study of trade barriers.
- The Secretariat will further refine its work on gas demand, particularly the effect of alternative price scenarios on demand.
- The Secretariat will assist Spain in a new study of a Gibraltar gas pipeline, and work on other project feasibility studies.

To further the Secretariat's work, the SLT agreed that countries would be asked to answer additional questions on gas as part of the 1983 IEA review of national energy programs. The Secretariat accepted our suggestions for questions to be included in this questionnaire. Our objective is for these questions to become a regular part of the annual national energy program reviews conducted by the Secretariat. The responses to the questionnaires should help us to identify potential changes in the pattern of supply of natural gas at an earlier stage than present, allowing time for full discussion of the security implications of such changes in a multilateral setting.

With the July 20 meeting, the work program of the SLT is off to a good start. The willingness of the members to accept the supplementary gas questionnaire is an encouraging sign of continued interest in energy security.

The work of the Secretariat outside of the country review process itself will provide other opportunities to discuss gas security. The Secretariat will continue to assist Spain in its efforts to spark interest in a feasibility study for a possible gas pipeline system to bring Nigerian and Algerian gas to Europe under the Strait of Gibraltar. We also will suggest that the Norwegians make another presentation to IEA members on the progress in the development of the Troll field. Finally, we will want to encourage more discussion of security improvements which IEA countries can make now, such as constructing gas storage facilities for strategic purposes over and above the new storage now being added mainly to meet the requirements of normal operations.

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Bilateral

The following countries and issues will be particularly important in the coming year:

Italy: The Italians are currently deciding how much additional Soviet gas to buy. Negotiations between Italy and the USSR have gone poorly. The Italians insist that they will buy no more Soviet gas without matching Soviet purchases of Italian goods and services with no concessions on Italian credit terms. The Italians are also pressing for a lower gas price than the Soviets are willing to offer. With Italian demand for gas flagging, Rome does not feel pressed to sign up new gas supplies, and Italian industrial exporters have, at least temporarily, relaxed their pressure for a new gas deal. As occasions arise, we should encourage the Italians in their current hard line. A Dutch decision to increase gas exports above current levels could provide Italy with a ready alternative to Soviet gas.

Norway: We will continue to encourage the development of the giant Troll gas field. We will have to take care, however, to avoid the impression that we are trying to manage Norway's resources. A presentation by Norway to the IEA on the Troll field would be especially appropriate if, as expected, Shell completes its declaration of commerciality for the block it operates.

Spain: Spain is still trying to spark interest in a possible gas pipeline system to bring Nigerian and Algerian gas to Europe under the Strait of Gibraltar. Other European countries, especially France, are skeptical about this idea and it has found little support in either prospective supplier country. There are also a number of practical difficulties which would have to be taken into consideration. Nevertheless, the Spanish pipeline is a possible alternative to Soviet gas. The Department of Energy is willing to provide up to \$500,000 toward a full feasibility study, if circumstances prove appropriate.

The Netherlands: The Dutch will soon complete an internal review of their energy policy, which may indicate a willingness to increase gas sales beyond the amounts in current contracts. Ambassador Galbraith has proposed a scheme for increased Dutch

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gas sales over the next decade, with the proceeds to be held in a trust fund for purchases of Norwegian gas once the Troll field is developed. Thus far, neither the Dutch nor the Norwegians have accepted this proposition.

France and Germany: We will be particularly interested to see whether these countries develop serious plans to increase gas storage capacity, over and above the storage needed for normal commercial operations. Both France and Germany have indicated unofficially, but clearly, that they intend to hold Soviet supplies to 25-30 percent of gas imports. We will continue to support the efforts of these two allies to minimize their reliance on Soviet-sourced energy.

Sweden: The USSR has proposed a pipeline through Finland to Sweden to supply Soviet gas to both countries. Finland already receives from the USSR all of the small amount (1bcm annually) of gas it uses. Sweden, however, is not a Soviet gas customer. Denmark currently supplies Sweden's minimal gas needs. We want to encourage the Swedes, perhaps via the Norwegians, to look to Norway rather than to the USSR for their future gas needs. In this regard, it is noteworthy that the Swedish State Power Board is promoting a proposal for a gas pipeline from the Tromsø field off northern Norway through Sweden to Denmark and Germany. The Swedes envision drawing up to 4 bcm of gas annually out of the proposed pipeline.

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